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Richard Madsen and Nancy A. Madsen v. Prudential Federal Savings & Loan Associations : Brief of Appellant

Utah Supreme Court

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IN THE SUPREME COURT
OF THE STATE OF UTAH

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RICHARD MADSEN and NANCY A. MADSEN, his wife, Plaintiff and Appellants, -vs- PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION, Defendant and Respondent.	)	CASE NO. 14530

---oooOooo---

BRIEF OF APPELLANT

APPEAL FROM THE JUDGMENT OF THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT IN AND FOR SALT LAKE COUNTY, STATE OF UTAH
HONORABLE BRYANT CROFT, DISTRICT JUDGE

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STATEMENT OF THE NATURE OF THE CASE

As part of a trust deed agreement, plaintiff-appellant (hereinafter Madsen), makes monthly "budget" payments to defendant-respondent (hereinafter Prudential). Prudential accumulates such "budget" payments and makes annual payments for taxes and insurance. Prudential has invested the "budget" funds without Madsen's knowledge or consent. Prudential has made substantial profits on such investments. Madsen contends that Prudential has been unjustly enriched by its unauthorized use of such "budget" payments.

RELIEF SOUGHT ON APPEAL

Madsen seeks to have the lower court's order granting Prudential's motion for summary judgment reversed, and the order denying Madsen's motion for partial summary judgment reversed, with the case remanded to determine the amount of the unjust enrichment and for further proceedings on the class action issues consistent with Honorable Bryant H. Croft's memorandum decision dated November 25, 1975 (which stayed the decision of granting or denying class action status until the question of liability is decided).

STATEMENT OF FACTS

During 1964, Madsen borrowed money from Prudential for the purpose of purchasing real estate. During the closing and as part of the financing arrangements, Madsen was required to sign a standard deed of trust prepared by Prudential (Exhibit 1 to plaintiff's Complaint). That document contained a provision requiring Madsen to pay, not only the monthly principal and interest payments, but also to pay monthly 1/12 of the estimated annual real estate taxes and insurance premiums into a "reserve" or "budget" fund for insurance and taxes. The language of the Deed of Trust is as follows:

> "A. To protect the security of the deed of trust, TRUSTOR agrees:
> . . .
>
> 2. To keep the buildings . . . insured against loss by fire . . . , and to pay the premiums therefor promptly when due . . .
>
> . . .
>
> 4. To pay before delinquent all taxes and assessments affecting said property. . . .
>
> "In addition to the monthly payments as provided in said note, the TRUSTOR agrees to pay to the BENEFICIARY, upon the same day each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to be adjusted from time to time as required, and said budget payments are hereby pledged to the BENEFICIARY as additional security for

> the full performance of this deed of trust and the note secured hereby. The budget payments so accumulated may be withdrawn by the BENEFICIARY for the payment of taxes or insurance premiums due on the premises. The BENEFICIARY may at any time, without notice, apply said budget payments to the payment of any sums due under the terms of this deed of trust and the note secured hereby or either of them. TRUSTOR'S failure to pay said budget payments shall constitute a default under this trust." (Emphasis added.)

At the time plaintiffs signed the deed of trust, they were aware of the "escrow" account which did not pay interest or earnings but did not object because this is a standard procedure with most lending institutions and Madsen had to agree to make the monthly budget payments for taxes and insurance with no interest or earnings or be refused financing. (Plaintiff's deposition at 26 and 47 cited in defendant's memorandum supporting summary judgment at 5.)

Intro. That the requirement of monthly payments for taxes and insurance is standard procedure for most lending institutions is evidenced by the federal regulations which require such budget payments on all mortgage loans exceeding 80 percent of value made by federal savings and loan associations. (§545.6-1(a)(4)(iii), C.F.R. 1974) and other similar regulations and statutes that compel or allow budget payments in other situations. The Code of Federal Regulations specifically provides that:

> [FHA mortgages] shall provide for such equal monthly payments by the mortgagor to the mortgagee as will amortize . . . the estimated amount of all taxes and fire and other hazard

insurance premiums . . . within a period
ending one month prior to the dates on
which the same become delinquent."
(§203.19, C.F.R., 1971)

A Federal Home Loan Bank regulation states:

"A federal association may require that an equivalent of one-twelfth of the estimated annual taxes, assessments, insurance premiums and other charges on real estate security be paid in advance . . . to enable the association to pay such charges as they become due from the funds so received. . . . "
(12 C.F.R. §545.6-11)

In addition, the Utah Code allows savings and loan associations to require such budget payments as follows:

"The association may require that the equivalent of one-twelfth of the estimated annual taxes, assessments, insurance premiums and other charges upon real estate security, or any of them, be paid each month in advance to the association in addition to interest and principal payments on its loans so as to enable the association to pay such charges as they become due from the funds so received. The association shall keep a record of the status of taxes, assessments, insurance premiums and other charges on all real estate on which the association has made loans or which is owned by the association." (U.C.A. §7-7-5(a)(3)).

The Deed of Trust provides in paragraph 4 that budget payments are pledged as security for performance of the Deed of Trust, and that such payments are to be used by Prudential to pay any amounts due under the Deed of Trust including payment of taxes and insurance premiums. Prudential holds such "budget" payments for up to one year before the taxes and insurance premiums are paid. Prudential engages a regular policy of investing those "budget" funds during the time they are in Prudential's possession, i.e., before the taxes and insurance premiums are paid. Prudential has earned a sizeable profit from its unauthorized use and investment of the Madsen "budget" funds.

PROCEDURAL BACKGROUND

Prudential's motion for summary judgment was granted and Madsen's motion for partial summary judgment was denied by the lower court on the 15th day of March, 1976. Madsen filed his notice of appeal on the 25th day of March, 1976.

POINT I

THE CONTRACTUAL ARRANGEMENT FOR DEFENDANT TO HOLD "BUDGET" PAYMENTS CONSTITUTES A PLEDGE.

Paragraph [illegible] attached to plaintiff's complaint, states as follows:

> . . . said budget payments are hereby pledged to the BENEFICIARY as additional security for the full performance of this deed of trust and the note secured hereby. The budget payments so accumulated may be withdrawn by the BENEFICIARY for the payment of taxes and insurance premiums due on the premises."

This language clearly creates a pledge. Not only does the instrument specifically use the word pledge, but it fulfills the two requirements of a pledge laid down by the Utah Supreme Court in Williams v. Esprey, 11 Utah 2d 317, 358 P.2d 903 (1961). Those two requirements are (1) the existence of a debt or obligation and (2) the transfer of personal property to the pledgee to be held as security and if necessary used for payment of the debt. The language of the Deed of Trust evidences a debt. Moreover, neither party to this lawsuit denies that defendants hold the mortgage on plaintiff's property and that a debt is thereby created. The second element is met by the express language of the Deed of Trust which states that the budget payments are to be held as additional security for its performance and that such payments may be applied against any amounts due thereunder.

Where the language of a contract ". . . is clear and is not susceptible of more than one interpretation, the ordinary plain meaning of the words must be used." Bryant v. Deseret News Publishing Co., 120 Utah 241, 233 P.2d 355 (1951); See also, Jensen's Used Cars v. Rice, 7 Utah 2d 276, 323 P.2d 259 (1958). Such is the case here as the language quoted above and the discussion following that quotation shows that the language of the Deed of Trust is unambiguous in creation of a pledge. In such a case, the rule requires that the plain meaning of the words be used. The plain meaning is that a pledge was created.

The law in Utah is clear that a pledgee who uses pledged property without the pledgor's authorization must account for any profits made because of such use in absence of a contrary agreement. Hoyte v. Upper Marvin Ditch Co., 94 Utah 134, 76 P.2d 234 (1938); see also, Leggat v.

Palmer, 39 Mont. 302, 102 P.2d 327, 329 (1909); Story on Bailments, §331. As stated by the Utah Supreme Court in Hoyte:

> ". . . when the property pledged is of such a character as not to be lessened by use, the pledgor does not incur liability by using it, but if from the use of it profits are derived, he must, in the absence of special agreement, account for them to the pledgor."

In the case at bar, no evidence can be found in the record of an agreement allowing Prudential to keep profits made on the escrow fund. No evidence is in the record because no such agreement, written or oral, was ever made. Plaintiffs did not agree nor does the Deed of Trust provide that Prudential can even use the budget payments except as security and for payment of amounts due under the Deed of Trust. Under the Hoyte doctrine, the absence of such an agreement requires Prudential, as pledgee, to account for profits made on the pledged escrow fund.

The rule stated above is also the one adopted universally in the United States today. See e.g. Thomas v. Waters, 350 Pa. 214, 38 A.2d 237, 241 (1941); Manuf. Trust Co. v. Bank of Yorktown, 282 N.Y.S. 507, 509 156 Misc. 793 (1935); State v. Nicely, 18 P.2d 503, 506, 171 Wash. 439 (1933); Restatement of Security §27 (1941). That this is the proper rule is evidenced by the fact that the Uniform Commercial Code, which has been adopted by every state except Louisiana, requires that any increase or profits on pledged property in the form of money must be remitted to the debtor or applied against the debt. U.C.C. §9-207. The comments under that section make it clear that it is a codification of the common law.

Not only is this the clear weight of authority in Utah and in the United States today, but the rule that a pledgor is entitled to the increase of profits from the pledged property has been a basic legal principal since ancient times. I. A. Rocurek and J. S. Wigmore, Sources of Ancient and Primitive Law 480, 481 (1915); Id. at 401, 4 S.P. Scott, The Civil Law, 196 97 n.1 (1932). The Code of Manu promulgated between 400 B.C. and 200 A.D. state that "the fool who uses a pledge without the permission of the owner, shall remit half of his interest, as a compensation for (such) use." The same principal is embodied in the Code of Hammurabi which is believed to be the oldest civilized code of law. I.A. Rocureck and J. S. Wigmore, Sources of Ancient and Primitive Law, 401 (1915).

As evidenced by the above discussion, the rule is universal that absent a contrary agreement a pledgee who uses pledged property must account to the pledgor for profits made through such use. It is universal because it is the only fair and just result. The pledgee has made his profit by charging interest on the money loaned to the pledgee. To allow him to reap additional profits through use of the pledged property would result in injustice. This is especially true when, as here, the contract is one of adhesion and the pledgor has no bargaining power to influence the matter. Such a basic universally accepted principal of fairness should not be overlooked by this court.

POINT II

IF THE COURT FINDS THE LANGUAGE OF THE DEED OF TRUST TO BE AMBIGUOUS, IT SHOULD CONSTRUE SUCH LANGUAGE AGAINST THE DEFENDANT DRAFTER.

If this court finds that the language of the Deed of Trust is not clear but is susceptible of more than one interpretation, it should find that the lower court erred by not construing the contract against the drafter, Prudential Federal, to find a contract of pledge. It is well established that Utah law requires an ambiguous or doubtful contract to be construed against the drafter. Wingets, Inc., v. Bitters 28 Utah 2d 231, 500 P.2d 1007 (1972); Skousen v. Smith, 27 Utah 2d 169, 493 P.2d 1003 (1972); General Mills v. Cragun, 103 Utah 239, 134 P.2d 1089 (1943). This is especially so when the contract is one of adhesion on a printed form with blanks for the parties to fill in and the drafter ". . . has the advantage of a lender of money." General Mills, supra at 1094. It is also true that the drafter of a contract cannot later change its wording but must accept and be bound to the words he chose. Skousen v. Smith, 27 Utah 2d 231, 493 P.2d 1003 (1973).

In the instant case, the Deed of Trust is a printed form drafted by Prudential Federal Savings and Loan Association, a lender of money. Such facts require that the document be construed against the defendant drafter. This is especially true in light of the fact that Prudential not only drafted the form Deed of Trust but used its superior bargaining power in requiring Madsen to sign it. In such a case, Madsen had no influence on the wording of the contract. The drafter is most at fault in creating the confusion, and he should likewise suffer the greater consequences.

The only way the Deed of Trust can be construed as not creating a pledge is if Paragraph 4 is either deleted or rewritten. Such action is certainly not allowable under Utah law, especially when the party to be benefited by such revision is the drafter of the document who chose the very language sought to be changed. In Skousen, supra at 1005, the Utah Supreme Court refused to delete the word "on" in a contract and substitute the word "of" in its place at the request of the defendant who drafted the writing. The court, at 1005, said it is ". . . elementary that parties may be bound by the language they deliberately used in their contract irrespective of the fact that it appears to result in improvidence. . . . " If the court would not allow deletion and substitution of one preposition in Skousen, surely it would be improper to delete or revise a whole paragraph in the instant case so as to find something other than a pledge. Prudential Federal chose the language of Paragraph 4 and the lower court erred by granting it summary judgment and not finding that a pledge exists between the parties.

POINT III

IF THE COURT FINDS THAT A PLEDGE DOES NOT EXIST, THEN A PRINCIPAL AGENT RELATIONSHIP IS PRESENT WHICH REQUIRES THE DEFENDANT TO ACCOUNT FOR PROFITS MADE ON THE BUDGET PAYMENTS.

The relationship between plaintiffs and defendant is best characterized as a pledge because that is what the Deed of Trust says it is. However, the relationship might also be described as one of agency. In Continental Bank and Trust Co. v. Taylor, 14 Utah 2d §70, 384 P.2d 796, 800 (1963), the Utah Supreme Court adopted the definition of agency found in the Restatement of Agency 2d §1 by stating as follows:

> "Agency is the fiduciary relation which results from the manifestation of consent by one person to another that the other shall on his behalf and subject to his control, and consent by the other so to act."

The court also said that the existence of an agency does not depend on the payment of a wage or fee by the principal to the agent. In addition, it is recognized that an agency can be created by conduct alone and no written agreement is necessary. Ramey v. Myers, 11 C.A. 2d 679, 245 P.2d 360 (1952); Anderson v. Thacker 76 C.A. 2d 50, 65, 172 P.2d 533 (1946).

The instant case falls under the definition of agency found in the Continental case above. Under the

Deed of Trust Madsen is required to pay for taxes and insurance. Rather than pay these amounts directly, Madsen turns over to Prudential each month 1/12 of the annual amount for insurance and taxes. Prudential is then bound by paragraph 4 of the Deed of Trust to use the funds received from Madsen to pay for insurance and taxes or other amounts due thereunder. Because Prudential is bound to use Madsen's money in a certain way, an agency relation is established. Note, the Mortgage Banking Process, 7 Houston L. Rev. 70, 85 (1969). Madsen is the principal and Prudential is the agent through whom the monies are transferred to third parties.

Establishment of an agency relationship puts obligations on the agent when dealing with the principal's property. One such obligation is that an agent who handles his principal's property cannot keep any profits made thereby, except for what he is entitled to in the way of compensation for his services. Adams v. Herman, 106 C.A. 2d 92, 234 P.2d 695 (1951); Savage v. Mayer, 33 CA.A 2d 548, 203 P.2d 9, 10 (1949); Steiner v. Rowley, 35 C.A. 2d 713, 221 P.2d 9 (1950)

This rule is stated at §388 of the Restatement of Agency 2d as follows:

> "Unless otherwise agreed, an agent who makes a profit in connection with transactions conducted by him on behalf of the principal is under a duty to give such profit to the principal."

Comment A to §388 makes it clear that an agent must give such profit to the principal even if it was not received in violation of his duty or loyalty.

The above discussion aptly describes the situation found in the present case. Plaintiffs paid budget payments to Prudential, not for Prudential's use but for the payment of amounts due under the Deed of Trust. In the capacity as the plaintiff's agent, Prudential was bound to act in a fiduciary capacity with respect to the funds held. Restatement of Agency 2d §13. Because Prudential breached its fiduciary duty as an agent by using the budget payments for investment purposes without the principal's consent, the law requires that Prudential turn such unfair profits over to their rightful owners, the plaintiffs.

POINT IV

THE BUDGET PAYMENTS CONSTITUTE A SPECIAL DEPOSIT REQUIRING DEFENDANTS TO ACCOUNT FOR PROFITS.

Additional support for the finding that Prudential Federal should account for profits made through investment of the budget payments can be found in the law of bank deposits. Bank deposits fall into two categories -- general and special. When money is deposited in a bank with no expressed intent that a special deposit be created, the funds are deemed to be held by the bank as a debtor to the depositor and the bank can commingle the funds with its own assets and use them as it wishes, 10 Am. Jur. 2d, Banks §§360, 364. No trust is created as a ". . . debt is not a trust." Restatement of Trusts 2d: Trusts §12. When money is left with a bank to be used for a specific purpose, such as payment of a debt or transfer to a particular person, a special deposit is created. Id. at §366. In such as case, ". . . the money does not become the property of the bank. The fund is merely entrusted to the bank as a trustee or bailee." Andrew v. Union Sav. Bank & Trust Co., 220 Iowa 712, 715, 263 N.W. 493, 497 (1935) Carpenter v. Suffolk Franklin Sav. Bank, Mass, 291 N.E. 2d 609 (1973); McGregor v. First Farmers'-Merchant Bank & Trust Co., 180 Wash. 440, 40 P.2d 144, 147 (1935); Engleman v. Bank of America Nat. Trust & Sav. Ass'n, 98 C.A. 2d 237, 219 P.2d 868 (1950).

The latter law governing special deposits controls the instant case. Specifically, Madsen deposited money with Prudential to be held for a particular purpose. Neither the parties nor the Deed of Trust disputes the fact that the budget payments were held by Prudential Federal for a particular purpose -- the payment of insurance and taxes or other amounts due under the Deed of Trust. Such facts created a special deposit with Prudential as the trustee or bailee and Prudential had no authority to use the funds as its own. Andrew, supra. Because Prudential Federal has violated its duty by taking these specially deposited funds and investing them, Prudential now owes Madsen an account for profits made thereby.

POINT V

DEFENDANT'S RETENTION OF PROFITS MADE ON ESCROW ACCOUNTS CONSTITUTES UNJUST ENRICHMENT AND AS SUCH SHOULD NOT BE ALLOWED.

The basic question in deciding whether defendant has been unjustly enriched is one of fairness. Applied to the present case the issue is whether it is more fair to allow Prudential Federal to retain the profits made by investment of the budget payments or whether those profits should be turned over to Madsen. Stated differently, would Prudential Federal be unjustly enriched if it were allowed to retain profits made on money deposited for the payment of insurance, taxes and other amounts?

The question above can be answered only by determining who is the owner of the profits. Ordinarily, profits belong to the one who expends efforts in earning them or the one who owns the capital or property producing the increase. (That use of another's property entitles the owner to a return is evidenced by rental payments made for the use of property and by interest paid for the use of money.) In this case, both are present. Prudential Federal has expended time and energy in administering the funds and it should be paid for such efforts. The owner of the funds however should also be compensated for the use of his property.

As Prudential used their own expertise, time, and effort in investing the funds, they should be compensated.

As the property invested was owned by Madsen, he is also entitled to be compensated. The profit made is correctly attributed to input received from both Madsen and Prudential. Without both -- the property and the investment efforts -- no profit would have been earned. The problem in this case is that Prudential is attempting to keep both the profit attributable to its managerial skills and the profit attributable to the use of Madsen's capital for itself.

An illustration of the magnitude of the unjust enrichment which lending institutions reap from investment of escrow accounts is detailed in a law review note entitled Lender Accountability and the Problem of Noninterest-Bearing Mortgage Escrow Accounts, 56 Boston University Law Rev. 516, 533 (1974) The author of that note points out that despite banking industry claims of no profits on escrow accounts, an independent study by the Massachusetts Commissioner of Banks indicates that banks in Massachusetts make a substantial profit on such accounts. Specifically, ". . . in 1971, the mutual savings banks collectively netted a profit of $4,000,000 and state cooperative banks earned close to a million dollars in profits." Id. at 535. The unjust enrichment at issue therefore is substantial as these figures illustrate. And these figures compose only the profits made for one year in one state. Certainly it is unjust to allow a practice which enables lending institutions to make profits for their relatively few shareholders at the expense of tens of thousands of mortgagors. This is especially true when overreaching, unequal bargaining power, and contracts of adhesion, unfair in and of themselves, are the methods used by the lenders which enables them to continue this practice.

As prevention against unjust enrichment, the court should require Prudential to account for profits made through investment of the escrow accounts and to pay Madsen the profits attributable to the use of their funds. Such relief has been advocated by several commentators in this area. Attack on Tax and Insurance Escrow Accounts in Mortgages, 47 Temple L.Q. 352 (1974); Lender Accountability and the Problem of Non-Interest-Bearing Mortgage Escrow Accounts, 54 B.U.L. Rev. 517, (1974); Payment of Interest on Mortgage Escrow Accounts; Judicial and Legislative Developments, 23 Syracuse L. Rev. 845 (1972).

In fashioning the relief for unjust enrichment, the court should remember that this is an equitable proceeding and as such, the court has broad power to tailor relief to the circumstances. Hecht Co. v. Bowles, 321 U.S. 321 (1944). If the Court determines that an accounting for past profits would be too burdensome on Prudential, the least that should be required is that profits on such funds should be paid to Madsen from the date of this opinion forward.

The court is reminded that Madsen is not asking for all of the profits made through investment of the escrow account. Indeed, Prudential is entitled to some of those profits as compensation for administering and investing the fund. Madsen asks only for the profits which rightfully belongs to them. This would include only the excess profits or the unjust enrichment. Madsen is aware that a decision on how the profits should be split may require that this case be remanded to the lower court for a determination of what Prudential is entitled to in the way of a reasonable management fee.

POINT VI

PRUDENTIAL'S ARGUMENT THAT A FINDING FOR MADSEN WILL CREATE HAVOC IN THE BANKING INDUSTRY IS UNFOUNDED.

Madsen anticipates that Prudential will argue as they did in their memorandum in support of their motion for summary judgment that a finding for Madsen which requires an accounting of profits made on these escrow accounts would create more problems than it would solve and that it would create havoc in and unduly burden the banking industry. Such contentions are unfounded. The Bank of America, the largest banking institution in the world, announced some time ago that it would begin paying the regular passbook savings rate of interest on mortgage escrow accounts (less the bank's cost of providing insurance and tax payment services) effective January 1, 1976. Los Angeles Times, Nov. 27, 1975, Part 3 at 18. Bank of America also stated that its decision would affect about 160,000 of its home mortgages.

> "B of A to Pay Interest on Mortgage Impound Funds in a major concession to California consumer advocates, Bank of America announced Wednesday that it will begin paying interest on home mortgage "impound" accounts -- the money banks and savings and loans often collect from homeowners to pay

insurance premiums and property taxes.

Beginning Jan. 1, 1976, the San Francisco-based bank said it would pay the regular passbook savings rate (currently 5% annually) on such accounts, less the bank's cost of providing insurance and tax payment services.

A spokesman for Bank of America said the service costs 'should run about 1%, leaving the homeowner with a net interest gain of approximately 4%.'

Bank of America would be the first major state lender to pay interest on impound accounts, although a number of large banks and savings and loan associations are known to have been considering such a move for many months.

'We've been looking at it for quite a while,' said an official with a rival California bank, 'and I know most of the other big banks have, too. Now that Bank of America has done it, I wouldn't be surprised if most of us followed suit pretty quickly.'

A number of consumer groups and state politicians have been urging banks and S&Ls to pay interest on impound accounts for several years, charging that the lenders benefited unduly from the use of their customers' funds.

Two separate pieces of legislation that would require banks and S&Ls to pay interest on such accounts currently are being considered in Sacramento.

In announcing its decision Wednesday, Bank of America said about 160,000 of its home mortgage accounts would be affected by the upcoming change, including FHA and VA loan accounts for which the collection of funds in anticipation of property taxes and insurance premiums is required by law.

Spokesmen for two large savings and loans in the Los Angeles area said they were 'surprised' by Bank of America's announcement. They said their firms would now be forced to consider similar plans."

If Bank of America can accommodate a policy change affecting 160,000 mortgages, certainly Prudential Federal can accomplish a similar change when only 20,388 mortgages are involved.

(p. 7 of defendant's Memorandum in Support of its Motion for Summary Judgment).

Moreover, the New York statutes were amended in 1974 to require all banks within that state to pay interest on mortgage escrow accounts effective April 1, 1974. McKinney's Consolidated Laws of New York, Banking Law §14-b (1974 Supp.). The state of New York which contains the greatest number, dollar wise, of banking institutions in the world has been requiring its banks to pay interest on mortgage escrow accounts for over two years and no great calamity has resulted.[1] If it can be done in New York, it can be done in Utah. Furthermore, bank trust departments routinely account for profits made on funds expressly held by them in trust. It should be no greater burden to require them to do so with mortgage escrow accounts. Defendant's cry of hardship is therefore unfounded as other banking institutions have been able to account for such profits.

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1. Other states also require payment of interest on escrow accounts and the banks involved have been able to do so without serious effects. See, Gen Stat of Conn. §33-10 (1975); A.C.M. §183:61; see also, Tierney v. Whitestone Sav. & Loan Ass'n, 77 Misc. 2d 284, 353 N.Y.S. 2d 104, 110 (Civ. Ct. Queens Co. 1974) where it is stated that similar legislation is expected to be adopted in Oregon, Minnesota, N. Carolina, Michigan, and Virginia.

POINT VII

PRIOR CASE LAW IN THIS AREA IS NOT CONTROLLING HERE.

The issue of whether a mortgagee's collection of impound accounts for insurance and taxes in connection with monthly mortgage payments imposes a duty upon the mortgagee to pay interest or account for profits made on such accounts has been the subject of increased litigation. See Carpenter v. Suffolk Franklin Savings Bank, Mass., 291 N.E. 2d 609 (1973); Buchanon v. Brentwood Federal Savings & Loan Ass'n., 457 Pa. 135, 320 A.2d 117 (1974); Abrams v. Crocker-Citizens National Bank, 41 Cal. App. 3d 55, 114 Cal. Rpt. 913 (1974); Surrey Strathmore Corp. v. Dollar Savings Bank, 36 N.Y. 2d 173, 325 N.E. 2d 527 (1975); Brooks v. Valley Nat'l Bank, _____ Ariz. ____________, 539 P.2d 958 (1975); Zelickman v. Bell Fed. Sav. & Loan Ass'n, 13 Ill. App. 3d 578, 301 N.E. 2d 47 (1973); Sears v. First Fed. Sav. & Loan Ass'n, 1 Ill. App. 3d 62, 275 N.E. 2d 300 (1971). The reason for the increased litigation in this area is very well stated by the following quote:

> "The concept of setting aside a pro-rata share of annual tax and insurance costs each month in a separate account arises from the experience of lenders during the depression of the 1930's, when many people lost their homes in tax fore-closures. In order to make mortgage loans more attractive to lenders, the Federal Housing Administration made escrow accounts mandatory on all FHA-insured mortgage loans. At that time, interest rates paid on savings accounts were so low - around 1 or 2 per cent - that no thought was given to payment of interest on escrow accounts.

In fact, some lenders charged an extra fee for handling the accounts. Over the years, the prepayment of tax and insurance payments into escrow accounts that bear no interest became established practice within the lending industry, not only for government-insured loans, but for conventional mortgage loans as well.

But times have changed, passbook interest rates are no longer at 1 per cent. The amount of money held in savings accounts is at an all-time high and the problem of tax foreclosures today is nowhere near what it was in the 1930's. As for the escrow funds lenders hold, it has become an accepted practice for many lenders to commingle these funds with other money invested for profit. Thus, the lenders have become accustomed to substantial income from the investment of mortgage borrowers' escrow funds, and seldom do they share those earnings with the people who own the money.

There are no national figures to show how much mortgage lenders earn from the interest-free use of escrow money, but a study of Prof. John A. Spanogle, Jr., of the University of Maine School of Law, estimates it at $100 million a year." "Homeowners v. Lenders - a Question of Interest", 38 Consumer Report 202 (1973).

Some, but not all, of the cases in this area have been decided adversely to the mortgagors. Plaintiffs anticipate that Prudential will rely heavily upon the following cases cited by Prudential to the lower court. Brooks v. Valley National Bank, 539 P.2d 958 (Ariz. 1975); Zelickman v. Bell Federal Savings, 301 N.E. 2d 47 (Ill. 1973). Madsen admits that a few cases have been decided in other jurisdictions which have considered similar issues and that such cases appear to support Prudential's position. Madsen, however, suggests that the court view Prudential's authorities from the following perspective:

(1) The highest court of a state is not bound by the decisions of other state courts but can choose to reject them all or accept and apply the reasoning which it feels best states the law. Ashton-Jenkins Co. v. Bramel, 56 Utah 587, 192 P. 273 (1920).
It is not even bound to accept the reasoning having a numerical majority. This is especially true when the issue involves a new and unsettled area of the law and the courts which have considered the matter are not in agreement.

(2) The cases favorable to Prudential's position are not controlling here as they all turned on the issue of a trust, Brooks at 961, and did not discuss the legal theories of pledge and agency which Madsen argues here. Indeed, Madsen is not even asking the court to decide the existence of an express trust.

(3) The primary issue before this court is the construction and interpretation of the Deed of Trust or contract between the parties. No court has ever considered the specific language contained in the Deed of Trust before this court. Only one case has been located which even contained a Deed of Trust with similar language, Zelickman v. Bell Fed. Sav. and Loan Ass'n, 301 N.E. 2d 47 (Ill. 1973) and that court

did not discuss the pledge theory. In accordance with the strong policy favoring freedom of contract, this court should not look to cases from other jurisdictions involving similar facts but different contract language. Instead, it should focus on the language of the Deed of Trust before the court.

CONCLUSION

The language of the Deed of Trust creates a common law pledge. Even if the language is ambiguous, it should be construed against the drafter, especially in a contract of adhesion. Since the "budget" funds were held by Prudential in pledge, Prudential must account to Madsen for any profit or increase which Prudential has earned by unauthorized use of the fund. This same result would prevail under the law of agency or banking fairness and equity demand that Madsen share in the profits which Prudential has earned by the unauthorized use of Madsen's property. The ruling of the lower court should be reversed.